Supreme Court, U.S.
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NO.

IN THE

Supreme Court of the United States

C. GREGORY EARLS,

Petitioner,

v.

UNITED STATES OF AMERICA,

Respondent.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

I. Particularly when considered as part of a recent trend of Second Circuit cases coming before it, should the opinion below be reviewed to determine whether the Second Circuit has now adopted such a vigorous and automatic "policy of inclusion" of any prior act evidence offered under Rule 404(b), that it allows such evidence even where *it is explicitly offered to show propensity*, and where its admission is not otherwise justified by any relevant purpose sanctioned by the Rule.

II. In this investment-fraud case, where petitioner Earls was charged with theft of investment monies from one specific venture (and no others), was Rule 404(b) disregarded in such a flagrant manner that this Court's review is required where, instead of limiting the evidence to any proof that petitioner stole the investment monies he had raised for the investment partnership as charged in the indictment, the Circuit Court affirmed, in a manifestly insouciant summary opinion, the following character/propensity assault on defendant:

(a) the district court allowed the prosecutors to introduce a torrent of evidence about "victims" of petitioner's past investment ventures that were not charged in the indictment, including 250 pages of testimony and 66 separate exhibits; and

(b) the district court itself questioned Earls extensively about these past ventures, and allowed the prosecutors to repeatedly refer to these uncharged investments as "past schemes," refer to the investors in them as "victims," show that many of these past investors had sued Earls on these past, uncharged investments, and even allowed the prosecutors to argue in closing that appellant Earls was guilty *on the charged scheme* because his "past schemes" showed

that "*he has done investment schemes like this before;*" and

(c) the district court allowed extensive evidence that appellant Earls had made various pledges to charities and then reneged on those pledges, and then allowed the prosecutors to elicit the testimony from one witness *that he (the witness)* had never reneged on any of *his* pledges to charities, in order to juxtapose that witness' having paid pledges as promised with appellant Earls' failure to pay as promised.

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OPINIONS BELOW

The Opinion of the Court of Appeals for the Second Circuit affirming the District Court's Judgment and Conviction is found in the Appendix ("App.") 1a-5a. The Order denying the rehearing is found at App. 6a. Various excerpts of the trial transcript showing what we contend to have been the unwarranted questioning about the propensity evidence by the Court itself are found at App. 8a through App. 11a.

JURISDICTION OF THIS COURT

The decision of the Court of Appeals and its judgment were entered on December 7, 2005. (App. 5a) A timely petition for rehearing was denied February 22, 2006. (App. 7a) This Court has jurisdiction pursuant to 28 U.S.C. § 1254.

FEDERAL EVIDENCE RULE INVOLVED

Rule 404(b) of the Federal Rules of Evidence provides in pertinent part as follows:

> **(b) Other Crimes, Wrongs, or Acts.**-- Evidence of other crimes, wrongs, or acts is not admissible to prove the character of a person in order to show action in conformity therewith. It may, however, be admissible for other purposes, such as proof of motive, opportunity, intent, preparation, plan, knowledge, identity, or absence of mistake or accident . . . .

STATEMENT OF THE CASE

I. Overview of the Charges, Earls' Defense, and the Other Act Evidence At Issue

A. *The State of the Stock Market*

The Indictment alleged that Earls and other investors formed "USV Partners" in 1998-99 and invested $20,000,000.00 in it so that Earls, as the general partner, could buy shares in U.S. Technologies, a publicly-traded company the stock of which was on the rise as part of the pre-2000, high-tech stock "bubble." *See*, Second Circuit Appendix ("A") 23. This high-tech "bubble" was, according to a government witness:

> . . . a time when almost every internet company that was ever formed went public on a wing and a prayer and they got tremendous valuations . . . and greed was running rampant on Wall Street and Main Street at that time.

[Trial Transcript "Tr." 1484] While the bubble still grew, Earls was the hero because the stock of U.S. Technologies he had purchased for his USV Partners skyrocketed.

In 2000, these "tremendous" valuations "started to decline precipitously" in the words of the same government witness. [Tr. 1485] The Second Circuit itself has noted "many technology companies that did not survive the bursting of the technology bubble during 2000." *P. Stolz Family Partnership L.P.* v. *Daum*, 355 F.3d 92, 95 (2d Cir. 2004).

When the bubble burst, unfortunately, the *normally-applicable*, legal restrictions prevented the USV Partners investors from selling their U.S. Technologies stock, even as they watched its value crater. For example [Tr. 1991]:

> So here's [INVESTOR] Warren. His stocks are at $12 million, he wants to hit the bid. I don't blame him, everyone would like to do that, but we were restricted. I had nothing to do with it, these were the security laws. I have to abide by them, everyone had to abide by them. So people were frustrated . . . they could not sell.

Earls became the goat.[1] The charges followed.

B. *The Charges in the Indictment*

The charge was that Earls, as general partner for USV partners, raised $20,000,000.00 to buy US Technologies stock and then stole $13.8 million of that:

> Earls engaged in a scheme to defraud investors of USV Partners, a company he controlled, by falsely representing that the company would use funds raised from investors to capitalize U.S. Technologies, a company of which he was chairman and CEO . . . [and then] misappropriated approximately $13.8 dollars . . . and used those funds for various undisclosed purposes, including to fund an educational trust for his children, to repay investors from other failed ventures, and to make deposits into his personal accounts.

---

[1] Federal law unarguably prevented for two years the resale of the newly-issued stock series purchased for most of the investors. As was acknowledged at sentencing, "COUNSEL: The shares were restricted. THE COURT: Yes. That is the problem." Sent. Tr. pp. 5 and 6. So Earls' hands were tied. He could not sell while the bubble burst and the stock slid.

(A 25-26) The prosecutor repeatedly told the jury that (Tr. 2405):

> This case is about what Mr. Earls told [USV Partners] investors he was going to do with the money and what he actually did with the money.

The District Court saw the case exactly the same way (Tr. 2115):

> The fraud here concerns making representations about what investments were going to be used for and not using the money for that purpose.[2]

C. *Earls' Defense*

Earls' defense was, simply put, that he did not steal the money. Instead, Earls testified that he had used $20,000,000.00 to buy the stock as promised and that he had the share certificates to prove it, ready to sell once the securities law would allow those sales. He pointed out that the audited financial records offered as exhibits by the government showed that it was impossible for him to have stolen this money since they showed that it had gone where promised. He also pointed out that before the bubble burst, everyone wanted more and more because the stock, while

---

[2] The supposedly missing $13.8 million dollars was thus the central charge, as the indictment and the comments of the court and the prosecutor make clear. Yet it was also alleged that he had made other, minor embellishments about who the investors would be and exaggerated the worth of the stock to be purchased. Two counts charged related frauds against specific investors. But as the trial progressed, these peripheral allegations played virtually no role, as the court and the prosecutor stressed that: "This case is about what Mr. Earls told [USV Partners] investors he was going to do with the money and what he actually did with the money." See text.

restricted, was soaring. For example, the indictment itself shows that the largest investor purchased *fourteen* different batches of the stock as he saw it rise. (A-28)

The case therefore should have gone to trial on the following question: did Earls steal the investment money as alleged? Instead, the trial became a veritable smear campaign involving Earls' past ventures and past conduct having nothing to do with the supposed "theft" of the USV Partners investment money. It became the trial of Earls, not the trial of the actions charged in the Indictment.

D. *The Use of Other Act Evidence*

1. The Other Act Evidence Summarized

Just before trial, the government announced to the court that:

> . . . we intend to offer at trial . . . that defendant: (1) between in or about December, 1995 and December, 1996, solicited and obtained funds from others for an investment in Pinheal Acquisition Co., Ltd ("Pinheal"); and Pinheal Corporation. (2) between in or about March, 1997 and December 1998 solicited and obtained funds from others in AVAC Holdings Ltd. ("AVAC"); . . . (4) failed to make charitable contributions he had pledged on behalf of [U.S. Technologies] to Master Chorale of Washington; and (5) failed to make charitable contributions he had pledged personally to Harvard University and the Boys and Girls Club of Washington D.C. The government intends to offer such

> evidence at the trial as evidence of the charges and/or background. In the alternative, the government would offer such evidence pursuant to Rule 404(b).

(A 56) All of this was allowed into evidence in droves.

2. The Prior Partnership "Schemes" known as Pinheal and AVAC

(i) Introduction. The prosecution spent a great deal of time on the two prior, uncharged investment ventures, called the "Pinheal" and "AVAC" investments. It repeatedly referred to Pinheal and AVAC as "prior schemes," its investors as "victims," and it went into excruciating detail of how Earls had misused funds from these two ventures, arguing (in opening and in closing): *"The first thing we know about Mr. Earls is that he has done schemes like this before."* (Tr. 2382-83) Their tactic, amplified below, shows that they went way beyond the proper use of those past ventures. It would have been one thing had the prosecution showed the existence of the past ventures and then attempted to show that Earls diverted monies from the venture he was charged with looting, USV Partners, to these prior ventures. That would certainly have been a proper way to show theft or diversion of USV Partner money, since it was all specifically earmarked for a new stock (US Technologies), not for old debts.

However, the government was allowed to go way beyond any proof of such a diversion, and instead was allowed to delve into the supposed underlying frauds involved in these past ventures, even though (1) no such fraud was charged, (2) the underlying facts related to those past ventures were not relevant to show the diversion charged in the indictment, and (3) Earls never made his intent his issue. His defense was never "I did not mean to do this; it was a mistake or

accident." Rather, he simply said that he had not diverted the money to pay the past ventures.

(ii) Past Ventures "Pinheal" and AVAC. Pinheal was a limited partnership formed by Earls in "1994 or 1995" (Tr. 1929) to purchase and hold certain shares of Franklin National Bank. The bank shares grew in value. (Tr. 1991-92) When Franklin was later acquired by another bank, the shares held by Pinheal "soared," and then "split." Investors then wanted their shares sold to reap the large profits involved. Since the stock had been pledged by Earls as collateral to allow him better borrowing power for various of his investments, it could not be sold at that time. This drew many complaints and many lawsuits from investors, though Earls claimed that they all got paid.

(iii) Past Venture AVAC. AVAC was a partnership Earls formed in 1998 (Tr. 1940) to purchase shares of Greyhound Bus Co. (Tr. 1936) Once he had acquired as many shares as he could, he used those shares to further the borrowing power of all of his investments. Then, a tender offer was made on the Greyhound shares by another company. The investors wanted their money from the proceeds paid by the purchaser, but it was at that time being used as collateral on various loans. Thus various AVAC investors were not paid right away. (Tr. 1942) They were angry and sued, although Earls claimed that they all got paid.

(iv) Earls' Defense to the Indictment. To the government charge that Earls had used USV Partners' money to repay AVAC and Pinheal investors, Earls' testified that the USV Partners money was not so used, but instead went as agreed to purchase US Technologies stock. He further explained that the repayments to AVAC and Pinheal were not made with any USV Partners money, but instead with the proceeds of sales of U.S. Technologies stock sold by Earls (who independently owned a series of the stock that was not restricted and thus could be sold), to the USV Partnership, and these proceeds were his to use.

The USV Partnership had the stock they had contracted to purchase, and the seller of that stock (Earls or anyone else) was free to do what he wished with the proceeds of those sales. So he used it to pay past debts.

Earls' defense presented the real issue for the trial, namely, where did the USV Partners money go? Yet this was drowned out by the wholesale airing of the details of the earlier AVAC or Pinheal investments.

3. The Use of AVAC and Pinheal to Argue Propensity

The government's effort to show propensity from the prior investments started in its opening statement, during which the prosecutor spoke of the supposed theft of USV Partners money:

> In fact, about $4 million went to pay off investors in two companies called Pinheal and AVAC. And these were two companies that the defendant had operated in the late 1990s, and he also victimized them by misusing investor funds.

(Tr. 47) The latter sentence simply was not relevant to prove the alleged diversion from the charged partnership, USV partners. If $4,000,000.00 of investment monies that Earls promised would be used to buy US Technologies Stock was in fact taken from the USV Partners' coffers to do *anything* but buy the stock it was put up to buy, that is obviously fraud and it mattered not whether the money was diverted to the Boys Scouts, or to a personal mansion for Earls to live in. It was a fraudulent diversion without *any* need to know the history of the allegedly wrongful transferee.

Yet this past "victimization" of the investors to whom this USV Partners money was supposedly

diverted was harped upon in the opening, during trial (by court and prosecutors) and in closing:

> Now I want to step back for a moment to give you an even bigger picture. Let's think about what is going on in these years from 1998 until 2000 and what we know about Mr. Earls. *Well, one of the first things that we know is that he's done investment schemes like this before.* He has set up limited liability companies whose sole purpose is supposedly to buy shares in a publicly traded company. You know that he set up Pinheal to purchase shares of Franklin National Bank, you know that he set up AVAC to purchase shares in Greyhound Lines.

(Tr. 2382-83) and:

> . . . in fact he [an investor] never invested in any of Earls schemes." (Tr. 2385) (emphasis added.)

and:

> He [Earls] gave the money to investors from previous schemes. (Tr. 2376) (emphasis added.)

and:

> . . . none of them[witnesses called by Earls] ever invested in any of Mr. Earls schemes. (Tr. 2403) (emphasis added.)

Between the opening and closing just discussed, the prosecution was relentless in its use of the prior "schemes." It started by informing the jury that it had given Earls' former secretary immunity for the AVAC and Pinheal "schemes" (Tr. 174):

Q. What's your [immunized witness'] understanding . . . under the [immunity] agreement?

A. It makes me exempt from prosecution for my participation in a scheme to defraud in the different entities.

Q. Which different entities?

A. AVAC, Pinheal, USV Partners and U.S. Technologies.

AVAC and Pinheal had never been the subject of any prosecution (not even for Earls, much less his secretary). Yet these prior ventures were surely made to look illegal and were used explicitly to argue that, because he had done them, he had likewise schemed in USV Partners, the only venture charged in the indictment.

Fully 66 exhibits were introduced on these past, uncharged investments, and 12 witnesses were asked about Pinheal or AVAC, their testimony consuming well over 250 pages of the 2500 page transcript. One witness was allowed to read from a demand letter he had written to Earls on the past AVAC venture:

A. Seven months ago, Laidlaw acquired Greyhound, the sole investment of AVAC holdings. Since that time, you have made regular assurances that that cash would be distributed to the investors. Typically, a distribution from the tender offer occurs in a matter of days. This one is seven months and counting. I understand the difficulties you have had with the preferred stockholders, this is an understandable delay, but not to the lengths that it has now gone.

Q. Turning to the second page, could you please read to us the first paragraph?

A. Two weeks ago in our telephone conversation you indicated that the funds would be sent out by the middle of the last week. I asked you point blank that, if that did not occur, would you use your own funds to meet that payment no later than last Friday. You agreed to do that. It is nearly a week later and I have not received these funds.

Q. What happened after you sent that letter to Mr. Earls?

A. Nothing.

(Tr. 120-121) Neither this letter, nor the AVAC investment discussed in it, had anything to do with whether or not Earl's had stolen the USV Partners investment monies that were the subject of the indictment; yet the whole sequence certainly made Earls look like a bad man. Not willing to leave even bad enough alone, the prosecutor then elicited from the same witness that, after Earls made an agreement to pay the witness on the earlier, uncharged investment, one of Earls' payment checks bounced. (Tr. 124)

When Earls was cross-examined, he was pounded about the past "schemes," in questions that switched back and forth between the charged conduct involving USV Partners, and the uncharged investment ventures of AVAC and Pinheal. He was examined in detail about the substance of the Pinheal investment, that was formed "in March 1995" (Tr. 2163), including (1) how he supposedly improperly borrowed on Pinheal assets and breached his "fiduciary responsibility" to the investors (Tr. 2162), (2) how he "commingled funds from the [Pinheal] venture" (Tr. 2163), and used its stock as collateral for a loan he made with the First Community Bank. *Id.* Once again, this had nothing to do with whether he had stolen money from a later venture, an allegation he denied through out.

Then the prosecution turned its guns on AVAC, the other uncharged investment partnership. (Tr. 2164) Earls was examined about two loans totaling "$1.4 million" that he had taken for his children's educational trust in "October 1996" and "November 1996," (Tr. 2165) and that "AVAC's shares in Greyhound Lines have been pledged on your . . . loan for $1.4 million." *Id.* The prosecutor then clearly used the AVAC and Pinheal ventures to make the propensity inference in relation to the charged USV Partners venture (Tr. 2165-66):

> Q. That loan [collateralized with assets from the earlier, uncharged AVAC venture and used for the educational trust] had nothing to do with Pinheal, did it?
>
> A. No.
>
> Q. It had nothing to do with AVAC did it?
>
> A. Not to my recollection, no.
>
> Q. It had nothing to do with USV Partners, did it?
>
> A. No.

Of course this 1996 loan from AVAC had nothing to do with USV Partners. By the Indictment's own allegation (A-23), USV Partners was formed "on or about June, 1998" and thus could have absolutely nothing to do with a loan made one full year earlier. The prosecutor's ploy was thus obvious: link the supposed wrongdoing from the prior ventures of Pinheal and AVAC to USV Partners to show that because he did it before, he did it again.

The prosecutor then was allowed to cross-examine Earls' extensively about lawsuits brought against him by AVAC and Pinheal investors, as well as by investors in even earlier ventures (not mentioned in the 404(b) notice and going as far back as 1993), which lawsuits obviously shed no light on whether Earls had stolen

money from the later USV Partners venture charged in the indictment. We set forth the entire sequence here since it reveals the tolerance now given for manifest efforts to smear a defendant using 404(b) in the most offensive way:

Q. And he [Richard Carella] invested personally?

A. In USV?

Q. In AVAC.

A. He did, yes.

Q. He also invested on behalf of the pension plan at his company, didn't he?

A. He did.

Q. He invested in AVAC starting in about February of 1998, isn't that right?

A. Yes.

Q. And throughout 1998, he invested a total of about $194,000, right?

A. I can't remember the exact amount.

Q. And he put in over $460,000 into USV Partners, correct?

A. I can't remember exactly.

Q. He filed a lawsuit against you in April of 2002, didn't he?

A. He did.

Q. And that lawsuit focused on his AVAC investments right?

A. Yes.

Q. That was filed four years after he invested in AVAC, wasn't it?

A. I don't remember the exact date.

Q. Are you also familiar with a man named John Bryant?

A. Yes.

Q. John Bryant is a former congressman from Texas?

A. He is.

Q. He invested in AVAC starting in February of 1998, right?

A. I don't remember the dates.

Q. He invested in AVAC?

A. He did.

Q. He invested a total of approximately $100,000?

A. That seems right.

Q. He filed a lawsuit against you in July of 2000, didn't he?

Q. That lawsuit focused on his AVAC investments, right?

A. Yes.

Q. We have heard about that lawsuit already because Billy Prince and Harold Warren were plaintiffs in that lawsuit, isn't that right?

A. That's correct.

Q. At that was filed over two years after they started investing in AVAC, wasn't it?

A. I don't think it was in the case of John Bryant. It was in the case of Billy Prince and Harold Warren, I believe.

Q. John Bryant started investing in AVAC in February of 1998, Didn't he?

A. I can't remember.

Q. The lawsuit was filed against you in July of 2000, correct?

A. I don't remember.

Q. You are also familiar with a man named Bruce Finland?

A. Yes.

Q. He distributes educational television programs and lives in Virginia, right?

A. Among other things, yes.

Q. He started investing with you in 1993, didn't he?

A. Yes.

Q. First he invested about $48,000 in National Networks, right?

A. Yes.

A. That's right.

Q. Then he invested about $200,000 in 1994 in Electronic Networks, right?

A. Yes.

Q. Then he invested $350,000 in Jayhawk in '94 and '95, right?

A. I don't remember the amounts, but I do recall him investing.

Q. And in 1995, he invested approximately $100,000 in Pinheal, didn't he?

A. I don't remember exactly, but I think he did invest, yes.

Q. He did invest in Pinheal?

A. My recollection he did, yes.

Q. In March 2001, Bruce Finland filed a lawsuit against you?

A. He did.

Q. Are you also familiar with George Marcus?

A. Yes.

Q. He is a real estate broker from Palo Alto, California?

A. He is.

Q. And in 1997, he invested $250,000 in AVAC, right?

A. Yes.

Q. And he filed a lawsuit against you in May of 2000, right?

A. Yes.

Q. He filed that three years after his last investment with you, isn't that right?

A. I don't remember the dates.

Q. You do remember that he filed a lawsuit against you?

Q. And that a short time after that you entered into a settlement agreement with him, isn't that right?

A. I did.

Q. And you defaulted on that settlement agreement, didn't you?

A. Ultimately I paid it, but I was late in paying it.

Q. Again, in November 2000, he filed yet another lawsuit against you for a breach of contract?

A. I can't remember that exactly, but I did default on the payments.

Q. And you remembered him filing another suit against you after that?

A. I don't recall, but we did ultimately pay it.

Q. Mr. Earls, Edward Eagles is a high school teacher at a school called St. Alban's, isn't that right?

A. Yes.

Q. And your sons sent to St. Alban's?

A. Yes.

Q. Mr. Eagles taught your sons?

A. Taught them all.

Q. In 1992 and 1993, he invested $25,000 in EDCO, didn't he, or Westcott Communications?

A. Yes.

Q. In 1993, he invested $200,000 in National Networks, isn't that right?

A. I think your numbers may be wrong on that. I think your numbers are wrong on the EDCO, but I am not sure. I can't remember. He did invest in EDCO. What was the next one you mentioned?

Q. National Networks?

A. He did invest in National Networks.

Q. He also invested in Jayhawk, didn't he?

A. He did.

Q. He also invested in Pinheal, right?

A. Yes.

Q. In 1995, isn't that right?

A. That's correct.

Q. In November 1999, he filed a lawsuit against you regarding Jayhawk, National Networks and Pinheal, didn't he?

A. That's my recollection, yes.

Q. Mr. Ackerman, as we know, was an investor in USV Partners, right?

A. Right.

Q. And he brought a lawsuit against you in 2002, right?

A. I believe he did, yes.

Q. Emmett Murphy was an investor in USV Partners?

A. He was.

Q. Mr. Murphy brought a lawsuit against you in 2002, right?

A. I think so.

Q. Arthur Hollingsworth was an investor of AVAC and USV Partners, Isn't that right?

A. Yes.

Q. Mr. Hollingsworth filed a suit against you, didn't he?

A. But not for USV Partners.

Q. He filed against you for AVAC?

A. Right.

(Tr. 2146-54) None of these lawsuits were germane to whether there had been a diversion of USV Partners funds. Moreover, the filing of civil claims is proof of very little. Indeed, the district court even backhandedly acknowledged this when, having allowed all of these unrelated lawsuits against Earls

into evidence from as far back as 1993, the court simultaneously refused to allow Earls to establish the scores of lawsuits filed against two of his chief witnesses, Ackerman and Ledecky, because: "How could we possibly cross-examine someone based on the filing of a civil complaint?" (Tr. 847) The Circuit Court opinion simply ignored this.

Last, and perhaps most damaging on AVAC and Pinheal, were the many harsh questions on the subject asked by the district court, which ultimately drew more attention to these investment schemes, and to the propensity use to which they were being put. All of these occurred as interruptions of the direct examination of Earls by his counsel, clearly signaling that the district court could not even wait for the prosecutor to cross-examine, and just as clearly signaling the court's dislike for what it believed Earls had done.

At Tr. 1929-1930:

THE COURT:	But why couldn't you take them [investors] out [of AVAC]?
EARLS:	Well, because they're collateralizing the loan.
THE COURT:	Well, what loan existed in 1997 against the facility?
EARLS:	I don't remember, your Honor, the exact amount, but it was several million dollars.
THE COURT:	But who was the borrower?
EARLS:	The borrower was -- I was the maker, the maker, myself, and an entity.
THE COURT:	Well, I'll let --

At Tr. 1930-1931:

THE COURT:	But not just in Pinheal, in many other transactions.
EARLS:	Yes, indeed, your Honor.
THE COURT:	So you were using the stock of Pinheal for other purposes which were not purposes which were exclusively for the benefit of the Pinheal investors; right?
EARLS:	Yes.

The district court's pointed prior act questioning is set out in more detail at App. 8a-11a. All of these questions related to the past, uncharged ventures and none had to do with the alleged stealing of money from the current venture to repay the prior ventures. By jumping in on direct examination about the prior investments, the court lent its credence to the propensity argument and certainly highlighted it.

4. Earls Failure to Pay Certain Pledges to Charities

The prosecutors then repeatedly elicited testimony that Earls had defaulted on pledges he had made to various charities (Tr. 2157-59):

Q. In 1997 you promised to contribute $75,000 to Harvard?

A. I don't remember the exact amount.

Q. You didn't pay that pledge did you?

This 1997 pledge had nothing to do with USV Partners' investment which did not even start until two years later "in or about June, 1999." Indictment,

¶2. Neither did the next charitable pledge Earls was asked about (Tr. 2156-57):

> Q. In 1998 you promised to contribute $100,000 to Harvard, didn't you . . .
>
> You did not pay that?

Going even further back in time, Earls was asked (Tr. 2158):

> Q. And in '95 or '96 you made $100,000 pledge to the University of Virginia . . . and you haven't paid anything on that pledge?

In closing the prosecutor repeated all of this and then noted that on one pledge, the charity had sent "five or six written forms to Mr. Earls to try to confirm his pledge." (Tr. 2401)

The intent to impugn Earls' character with failed pledges was clear when witness Strike, another Harvard contributor, was asked by a prosecutor (Tr. 2055):

> Q. "Did <u>you</u> always honor <u>your</u> pledges that you made for the Harvard Parents Fund?
>
> A. Yes.

Obviously, witness Strike's honoring of his pledges had nothing whatever to do with Earls' intent to defraud USV Partners investors by stealing their investment monies, but it did serve to juxtapose the good (witness Strike) with the bad (defendant Earls) and that was <u>precisely</u> the government's aim.

5. The Circuit Court's Affirmation of the Trial Court

In two pages of "Summary Opinion," the Circuit panel dismissed all of the other act evidence by simply mouthing certain buzzwords that have now become, literally, the "cookie-cutter" approach it has taken for the last decade in order to reject (see further below) virtually all challenges under Rule 404(b).

To begin with, it simply ignored Earls' denial that there had been any misappropriation of the investment monies, much less the allegation (never proven) that a full $13.8 million was stolen. It thus did not apply settled law holding that where defendant denies doing the charged act, prior similar acts are not admissible to show his motive or intent since they are not the issue because "defendant did not claim that he had taken the money innocently or mistakenly, but that he had not taken it at all." *United States* v. *Colon*, 880 F.2d 650, 657 (2d Cir. 1989). Instead of dealing faithfully with that denial and its bar to the use of prior acts to show intent and motive, the Second Circuit completely ignored Earls' defense in a fully Kafkaesque manner, namely, by stating that prior acts are admissible to show motive and intent where the defendant is arguing innocent mistake, *rather than when he is arguing "that he did not do the charged act at all."* (App. 4a) Yet this is precisely what Earls had argued by denying that he had stolen the money. Thus the repeated references to "past victims" and "past schemes," and the argument that "he has done schemes like this before," served the illicit propensity purpose, not some more nuanced argument about his intent or motive. Simply saying that evidence is used to show intent is not enough. At least that is what the Second Circuit used to hold:

> The government must do more than disclaim an intention of proving that the defendant is a bad man. For what

> prosecutor in his right mind will ever offer that improper justification. Instead, the prosecutor must show that the evidence is relevant, and there is no presumption that it is.

United States v. *O'Connor*, 580 F.2d 38, 40 (2d Cir. 1978). Now, instead of actually requiring a showing of a legitimate purpose for prior act evidence, the Second Circuit sustains its use if the government simply uses magic "buzz words."

The Second Circuit acted similarly when it held that the evidence of the underlying wrongdoing connected with the past, uncharged investment partnerships (AVAC and Pinheal) "completed the story of the crime on trial by clarifying for the jury *how* Earls' misappropriated funds from USV Partners in order to return funds to investors from his prior ventures." (App. 3a-4a) Once again, the panel decision simply mouthed a recognized exception (namely, "complete the evidence"] even though nothing about the underlying facts of the past investments could possibly have served that purpose. After all, showing "*how Earls' misappropriated funds from the USV Partners venture in order to return funds to investors from his prior ventures*," takes the form of checks or wire transfers drawn on USV Partners accounts yet payable to some other payee, rather than for the promised purpose of buying US Technologies' stock. It does not require any showing about how Earls had treated other investors in the past, nor endless talk of lawsuits filed by such earlier investors, nor calling past ventures "schemes" with "victims," nor exhortations that "Earls has done investment schemes like this before." Simply put, the past ventures were detailed because they were dirty, not because they were "necessary." Indeed they were not.

The same is true concerning the evidence that Earls' had reneged on promises to fund various charities. There is no legally acceptable argument that

starts with "*Earls promised to pay charities and then did not do so,*" which ends with "*thus ladies and gentlemen of the jury he did in fact steal $13.8 million from USV Partners.*" The Second Circuit did not even pretend that this was a fair argument. Instead it simply called the charities fraud evidence "*unimportant in relation to everything else the jury considered.*" (App. 4a) The just-quoted phrase is yet another hollow refuge, considering that the prosecutors referred to this evidence many, many times during the trial, and even in its closing.[3]

REASONS FOR GRANTING THE WRIT

A. Importance of the Rule

Rule 404(b) is important. It "has generated more reported decisions than any other subsection of the Federal Rules."[4] Such frequent use requires this Court's intervention to remind the Second Circuit that:

> . . . the task of the judge is to keep a sense of proportion, and he should

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[3] See, *United States* v. *Gordon*, 987 F.2d 902, 908-09 (2d Cir. 1993) "The government urged the jury to consider [under 404(b)] Gordon's possession of the 3.8 grams of crack and the triple-beam scale *both in its main summation and its rebuttal summation.* We can hardly conclude that the crack-possession evidence was "*unimportant in relation to everything else the jury considered.*" See also, *United States* v. *Ventura-Cruel*, 356 F.3d 55, 64 (1st Cir. 2003), noting that the parties use the important evidence in closing because "[closings] are the last words spoken to the jury by the trial attorneys." *Id. quoting United States* v. *Manning*, 23 F.3d 570, 575 (1st Cir. 1994).

[4] Professor Edward J. Imwinkelried, The Plan Theory for Admitting Evidence of the Defendant's Uncharged Crimes: A Microcosm of the Flaws in the Uncharged Misconduct Doctrine, 50 Mo.L.Rev.1,2.

> exclude such evidence 'where the minute peg of relevancy will be entirely obscured by the dirty linen hung upon it.'[5]

As the late Mr. Justice Jackson noted, courts "disallow resort by the prosecution to any kind of evidence of a defendant's evil character to establish a probability of his guilt." *Michelson* v. *United States*, 335 U.S. 469, 475-76, 69 S.Ct. 213, 93 L.Ed 168 (1948). Otherwise prosecutors will literally flood the trials with anything that has some fig-leaf sized alternate justification for admission (and sometimes not even that) in order to make their prey an irredeemably bad person. This invites the jury to "give way to the emotional impulse to punish because the other act alone shows that punishment is deserved." MUELLER and KIRKPATRICK, *supra*, § 107, p. 585. Such evidence can "so over persuade . . . as to prejudice one with a bad general record and deny him a fair opportunity to defend against a particular charge." *Id.* § 100, at p. 543. This, we contend, is precisely what was allowed at the Earls' trial and sustained by an overly-permissive Second Circuit which has lost the proper balance under Rule 404(b). A course correction is required.

B. Circuit Conflict

The Second Circuit used to follow the Rule:

> We share appellant's concern about the danger of unfair prejudice associated with the use of similar acts evidence. . . . district courts must exercise great care to ensure that juries are not permitted to conclude that because a defendant has

---

[5] MUELLER and KIRKPATRICK, Federal Evidence, § 100, p. 541 (Lawyer's Coop. Pub. 2d. Ed. 1994), *citing and quoting United States* v. *Bradwell*, 388 F.2d 619, 622 (2d Cir. 1968).

> committed a similar crime before, he or she therefore has a criminal propensity sufficient to justify conviction in the case at hand.

Colon, supra, 880 F.2d 650 at 656. [6]

Not only has the Second Circuit erased the line between the permissible and the impermissible (virtually all recent cases waive in whatever other act-evidence has been proffered),[7] creating a conflict in the case law, it compounds the problem by also no longer giving any meaningful consideration to the Rule 403 requirement that there be a balancing of the probative value of the offered prior-act evidence against any substantial unfair prejudice.

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[6] When decided in 1989, *Colon* was in line with the pronouncements of this Court and all the Circuits, under which the wholesale smear engaged in by the prosecutors at Earls' trial would not have been allowed. *See, Johnny Lynn Old Chief* v. *United States*, 519 U.S. 172, 181 (1997):

> The state may not show defendant's prior trouble with the law, specific criminal acts, or ill name among his neighbors, even though such facts might logically be persuasive that he is by propensity a probable perpetrator of the crime.

See also, United States v. *Victor Arias-Montaya*, 967 F.2d 708, 709 (1st Cir. 1992); *United States* v. *Michael J. Morley II*, 199 F.3d 129, 133 (3rd Cir. 1999); *United States* v. *Yitschak Ebert*, 178 F.3d 1287 (4th Cir. 1999); *John Panzavecchia* v. *Louie L. Wainright*, 658 F.2d 337, 341(5th Cir. 1981); *Washington* v. *Hofbauer*, 228 F.3d 689, 699 (6th Cir. 2000); *United States* v. *Earlie Brown*, 34 F.3d 569, 573 (7th Cir. 1994); *United States* v. *Johnson*, 439 F.3d 884 (8th Cir. 2006); *United States* v. *Kevin Patrick McCourt*, 925 F.2d 1229, 1232-33 (9th Cir. 1991); *United States* v. *Donnie Collins*, 97 Fed. Appx. 818, 826 (10th Cir. 2004); and *United States* v. *Nixon*, 918 F.2d 895 (11th Cir. 1990).

[7] See, e.g., *United States v. LaFlam*, 369 F.3d 153, 156 (2d Cir. 2004); *United States v. Edwards*, 348 F.3d 168, 176 (2d Cir. 2003); and *United States v. Garcia*, 291 F.3d 127, 136 (2d Cir. 2002), all of which, under the broad banner of the "inclusionary policy" waive in other-act evidence without anywhere near the same caution or circumspection it used in the past, or instructed in the decisions of this Court.

It used to do so. *See, Gordon, supra*, 987 F.2d 902, 908-09, (cited *supra* at note 3] reversing a narcotics smuggling conviction because the district court had allowed admission (under 404(b) of evidence that 16 months prior to the smuggling charged in the indictment, the defendant had smuggled "a modest amount of crack and a triple-beam scale." *Id.* at 909. In reversing, the Second Circuit gave proper deference to the potential harm of other act evidence and adhered to this Court's protective, balancing formula set forth in *Huddleston* v. *United States*, 485 U.S. 681, 687-88, 108 S.Ct. 1496, 1499-500, 99 L.Ed.2d 771 (1988), which it cited *id.*, at 987 F.2d 902, and followed, *id.*, at 909:

> We conclude (a) that Gordon's possession 16 months earlier of a modest amount of crack and a triple-beam scale had so little value to prove his knowledge that Ghullkie, whom he had met only recently, was importing a large quantity of cocaine and marijuana that it was inadmissible under Rule 404(b) and that in any event, the probative value of the crack possession was easily outweighed by its potential for unfair prejudice and the evidence therefore should have been excluded under Rule 403. Accordingly, we conclude that admission of that 1990 possession was an abuse of discretion.

This previous care has now been jettisoned and in its place is "an inclusionary rule." *United States* v. *Carboni*, 204 F.3d 39, 44 (2d Cir. 2000), *quoting*, *United States* v. *Gonzalez*, 110 F.3d 936, 942 (2d Cir. 1997). While the cases just cited state a nominal deference to the need to vet such evidence for propensity, and to effect a proper balance, this is now by rote formula, as the Earls' case makes plain. All the

district court said about the massive quantities of evidence discussed herein was:

> THE COURT: . . . I didn't regard the evidentiary material recited in the government's March 5 letter as actually constituting 404(b) material, that I found it to be essentially part of the government's case in chief. That even if I found it to be 404(b) material, I would find it admissible under the variety of exceptions to other bad acts evidence, and even if I reached a 403 analysis, I would find that the material is not unduly prejudicial.

(Tr. 14-15) That was it. There was not even an attempt to feign a real balancing analysis or any real explanation. The words were simply mouthed, not applied in any real sense.

Compounding all the rest of the relaxations of the Rule's safeguards, the Second Circuit now tolerates a "limiting" instruction that does more harm than good. With all the evidence dumped into Earls' trial, and the closing arguments stressing it still ringing in their ears, the jurors were instructed that: "you may not conclude that *because the defendant has committed crimes in the past*, he has probably committed this crime." (Tr. 2511) (emphasis added) If the jury had not understood before this damning instruction that the district court thought Earls to be a criminal from the prosecution's repeated propensity argument, or from the court's own accusatory questions about the prior conduct, this backhanded "limiting instruction" certainly drove that message home.

Rule 404(b), as originally formulated, is now gone in the Second Circuit, just as surely as if the Second Circuit had simply declared frontally its unwillingness to follow it any longer. This presents a conflict with the prior cases of this Court and those of the Circuits.

The issue should be considered by this Court given the common use in all the Circuits of prior act evidence.

CONCLUSION

Certiorari should be granted.

Respectfully submitted,

JOHN J.E. MARKHAM, II
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Dated: May 16, 2006

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APPENDIX A

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

SUMMARY ORDER

THIS SUMMARY ORDER WILL NOT BE PUBLISHED IN THE FEDERAL REPORTER AND MAY NOT BE CITED AS PRECEDENTIAL AUTHORITY TO THIS OR ANY OTHER COURT, BUT MAY BE CALLED TO THE ATTENTION OF THIS OR ANY OTHER COURT IN A SUBSEQUENT STAGE OF THIS CASE, IN A RELATED CASE, OR IN ANY CASE FOR PURPOSES OF COLLATERAL ESTOPPEL OR RES JUDICATA.

At a stated term of the United States Court of Appeals for the Second Circuit, held at the Thurgood Marshall United States Courthouse, at Foley Square, in the City of New York, on the 7 day of Dec two thousand and five.

PRESENT:

AMALYA L. KEARSE,
RICHARD J. CARDAMORE,
JOSÉ A. CABRANES,
Circuit Judges.

----------x

UNITED STATES OF AMERICA,

Appellee,

v. No. 05-1493-cr

C. GREGORY EARLS,

Defendant-Appellant.

----------x

APPEARING FOR APPELLANT:

JOHN J.E. MARKHAM, II, Markham & Read, Boston, MA

APPEARING FOR APPELLEE:

WILLIAM J. STELLMACH, Special Assistant United States Attorney (Karl Metzner, Assistant United States Attorney, *of counsel*, Michael J. Garcia, United States Attorney for the Southern District of New York, *on the brief*), United States Attorney's Office for the Southern District of New York, New York, NY

Appeal from a judgment of the United States District Court for the Southern District of New York (Naomi Reice Buchwald, *District Judge*).

UPON CONSIDERATION WHEREOF, IT IS HEREBY ORDERED, ADJUDGED, AND DECREED that the judgment of the District Court is AFFIRMED.

Defendant-Appellant C. Gregory Earls appeals from a judgment of conviction entered on March 2, 2005 in the District Court following a jury trial at which Earls was found guilty of securities fraud, wire fraud, and mail fraud. The District Court sentenced Earls principally to 125 months' imprisonment and three years' supervised release, and it ordered him to pay $21,971,628 in restitution. We assume the parties' familiarity with the facts and procedural background of this case.

On appeal, Earls asserts, *inter alia*, that the District Court (1) improperly admitted evidence of previous investment schemes and other conduct unrelated to the crimes charged in the indictment, thereby encouraging the jury to draw impermissible "propensity" inferences based on Earls's prior bad

acts, (2) improperly questioned Earls in a manner that *signaled to the jury the Court's skepticism of* Earls's testimony and defense, and (2) erred in sentencing Earls by improperly relying on an "emotional letter submitted by an investor who blamed Earls for the trauma [Earls] cased," Br. Of Def.-Appellant at 45.

We review a district court's evidentiary rulings for abuse of discretion, *see United States v. Taubman*, 397 F.2d 161, 164 (2d Cir. 2002), according "[p]articular deference . . . to a ruling of the trial judge with respect to relevancy" because the trial judge "has a familiarity with the development of the evidence and the jury's reaction to it which an appellate court cannot equal," *United States v. Southland Corp.*, 760 F.2d 1366, 1375 (2d Cir. 1985). With regard to evidence offered pursuant to Federal Rule of Evidence 404(b), "[w]e follow an inclusionary rule, allowing the admission of such evidence for any purpose other than to show a defendant's criminal propensity, as long as the evidence is relevant and satisfies the probative-prejudice balancing test" set forth in Federal Rule of Evidence 403. *United States v. Inserra*, 34 F.3d 83, 89 (2d Cir. 1994). Evidence of prior criminal activity may be admitted, even if uncharged, where it "arose out of the same transaction or series of transactions as the charged offense, if it is inextricably intertwined with the evidence regarding the charged offense, or if it is necessary to complete the story of the crime on trial." *United States v. Carboni*, 204 F.3d 39, 44 (2d Cir. 2000).

Upon our review of the record, we hold that the District Court did not abuse its discretion by admitting evidence that Earls participated in two prior investment schemes that strongly resembled USV Partners—the investment vehicle that Earls used to defraud investors of over twenty million dollars—because evidence of these schemes "complete[d] the story of the crime on trial" by clarifying for the jury

how Earls "misappropriate[ed] funds from USV Partners in order to return funds to investors from his prior ventures, [and] at times converted the profits due these investors into an equivalent interest in USV Partners. . . . without ever seeking authorization from the actual investors of USV Partners." Indictment ¶ 31. [A 32] Moreover, evidence concerning Earls's past investment schemes was highly probative of Earls's motive and intent to defraud investors, both of which were contested at trial. *See United States v. Colon*, 880 F.2d 650, 657 (2d Cir. 1989) (distinguishing between "defense theories that claim that the defendant did not do the charged act at all, and those that claim that the defendant did the act innocently or mistakenly").

With respect to Earls's argument that the District Court improperly admitted certain evidence of other "bad acts" unrelated to Earls's investment ventures—such as his reneging on financial commitments to various nonprofit institutions—we hold that the admission of such evidence was, at worst, harmless error because the challenged testimony was "'unimportant in relation to everything else the jury considered on the issue in question, as revealed in the record.'" *United States v. Rea*, 958 F.2d 1260, 1220 (2d Cir. 1992) (quoting *Yates v. Evatt*, 500 U.S. 391, 403 (1991)). As the District court correctly noted, the evidence introduced by the Government to establish Earls's guilt was "overwhelming"; accordingly, we hold that the errors alleged by Earls on appeal were harmless inasmuch as they did not "substantially sway[]" the jury's verdict. *Kotteakos v. United States*, 328 U.S. 750, 765 (1946).

Defendant's contention that the District Court improperly questioned Earls in a manner that signaled to the jury its skepticism of Earls's testimony is similarly unavailing. Despite Earls's contention that the tone of the court's questions was "accusatory," Br.

of Def.-Appellant at 2, Earls did not object to any of the court's questioning; indeed, in one exchange, his attorney stated, "I think your Honor's questions are exactly the ones that I was going to ask." Given that the court's questions appear to have been designed to clarify Earls's testimony, rather than to favor the prosecution, we cannot say that the questioning "so impressed the jury with the trial judge's partiality to the prosecution that this became a factor in determining the defendant's guilt." *United States v. Pisani*, 773 F.2d 397, 402 (2d Cir. 1985). Accordingly, we hold that if there was error, it was not plain. *See United States v. Livoti*, 196 F.3d 322, 326 (2d Cir. 1999) (reviewing for plan error where defense counsel failed to object to allegedly improper question posed by the trial court).

Upon our review of the District Court's sentencing proceeding, we find no error in the District Court's alleged "reliance" on a victim impact letter. The District Court properly calculated a Guidelines sentence, took into account the other factors set fourth in 18 U.S.C. § 3553(a), and imposed a reasonable sentence, albeit one that was *below* the applicable Guidelines range for Earls's offense.

* * * *

We have considered all of Earls's arguments and found each of them to be without merit. Accordingly, the judgment of the District Court is AFFIRMED.

FOR THE COURT,

Roseann B. MacKechnie, Clerk of Court

By: /s/Lucille Carr

APPENDIX B

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT
THURGOOD MARSHALL U.S. COURT HOUSE
40 FOLEY SQUARE
NEW YORK 10007

Roseann B. MacKechnie
CLERK

Date:	2/15/06
Docket Number:	05-1493-cr
Short Title:	USA v. Earls
DC Docket Number:	03-cr-364
DC:	SDNY (NEW YORK CITY)
DC Judge:	Honorable Naomi Buchwald

At a stated Term of the United States Court of Appeals for the Second Circuit, held at the Thurgood Marshall United States Courthouse, Foley Square, in the City of New York, on the 22nd day of February two thousand six.

Present:

Hon. Amalya L. Kearse

Hon. Richard J. Cardamone

Hon. José A. Cabranes,

CIRCUIT JUDGES.

USA v. Earls 05-1493-cr

A petition for panel rehearing having been filed herein by C. Gregory Earls

Upon consideration thereof, it is

Ordered that said petition be and it hereby is DENIED.

For The Court,

Roseann B. MacKechnie, Court

By: /s/_____
Motion Staff Attorney

APPENDIX C

EXCERPTS OF DISTRICT COURT'S QUESTIONING OF EARLS ABOUT PRIOR, UNCHARGED INVESTMENTS

At Tr. 1929-1930:

THE COURT:	But why couldn't you take them [investors] out [of AVAC]?
EARLS:	Well, because they're collateralizing the loan.
THE COURT:	Well, what loan existed in 1997 against the facility?
EARLS:	I don't remember, your Honor, the exact amount, but it was several million dollars.
THE COURT:	But who was the borrower?
EARLS:	The borrower was -- I was the maker, the maker, myself, and an entity.
THE COURT:	Well, I'll let --

At Tr. 1930-1931:

THE COURT:	But not just in Pinheal, in many other transactions.
EARLS:	Yes, indeed, your Honor.

THE COURT: So you were using the stock of Pinheal for other purposes which were not purposes which were exclusively for the benefit of the Pinheal investors; right?

EARLS: Yes.

At Tr. 1931-1933:

THE COURT: But restrictions expire after a year, or you get an opinion of counsel, and then that stock becomes freely tradable.

EARLS: Not necessarily, your Honor, if you're an insider. For example, in Westcott Communications or Jayhawk, if I were a director and a founder and an officer, then I can only sell at certain times of the period.

THE COURT: But Holly Miscreants is not an insider.

EARLS: Well, in Franklin Bank Corp I was an insider, but she doesn't have her shares. If I'm holding on her behalf, she has the same restrictions as I do.

THE COURT: Well, but what's the point then in making an investment in which you can't ever sell the stock because you're holding it in a fashion that makes it restricted?

EARLS: Because at some point those restrictions come off, and usually at some point when those restrictions will come off one will be able to sell.

THE COURT: But Pinheal was formed in 1994 and Ms. Miscreants didn't have her money until 2002.

BY MR. COBURN:

Q. So you how was that?

THE COURT: How do you explain -- restrictions don't last that long, even if they're different timetables for them to come off.

BY MR. COBURN:

Q. So what happened?

A. First of all, Franklin Bank Corp had no restrictions, I didn't have any restrictions, I wasn't an officer, I didn't own more than

five percent, and I didn't have any restrictions on the Pinheal.

THE COURT: So why didn't you just sell the stock and give the people who invested in Pinheal their money back?

EARLS: Well, that's a big question. What I mean is that depends on when you're asking the question.

THE COURT: Well, the point --

EARLS: Maybe at the time that -- maybe it wasn't time to sell. We had some people that wanted to sell at 11, in fact they forced me to buy their shares. I didn't want to sell at 11 and I couldn't sell.

THE COURT: But it's their money, not you're money; isn't it?

EARLS: No, it's in the partnership. It's my decision when to sell, not theirs.